

ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: Thomson Analyst: Kristina E. North Bill Number: AB 816
Related Bills: See Legislative History Telephone: 845-6978 Introduced Date: February 22, 2001
Attorney: Patrick Kusiak Sponsor: Franchise Tax Board

SUBJECT: Modify Filing Requirement Threshold to Allow Exclusion of Gain on Sale of Principal Residence

SUMMARY

This bill would repeal the income tax return filing requirement triggered solely by the sale of a principal residence where an individual's income otherwise is below the filing threshold.

PURPOSE OF THE BILL

The Franchise Tax Board (FTB) is sponsoring this bill to eliminate the requirement of having to file returns when no tax is owed.

EFFECTIVE/OPERATIVE DATE

This bill is a tax levy and would be effective immediately upon enactment and operative for taxable years beginning on or after January 1, 2001.

POSITION

Support.

At its December 18, 2000, meeting, the Franchise Tax Board voted 2-0 to sponsor the language introduced in this legislation.

ANALYSIS

FEDERAL/STATE LAW

Under **current federal and state laws**, an unmarried individual may exclude from income up to \$250,000 (up to \$500,000, if married) of gain realized on the sale or exchange of a principal residence. The individual must have owned and used the residence as a principal residence for a total of at least two of the five years prior to the sale or exchange. The exclusion may be used only once every two years.

When determining the filing requirement, **federal and state laws** specify that gross income must be computed without regard to the exclusion for the sale or exchange of a principal residence.

Board Position:

<u> X </u> S	<u> </u> NA	<u> </u> NP
<u> </u> SA	<u> </u> O	<u> </u> NAR
<u> </u> N	<u> </u> OUA	<u> </u> PENDING

Department Director

Date

Alan Hunter for GHG

04/04/01

THIS BILL

This bill eliminates the requirement to include excludable gain from the sale or exchange of a principal residence when computing gross income. This bill, for some taxpayers, would eliminate the requirement to prepare and file a return that would do nothing more than report excludable gain that is not subject to tax.

IMPLEMENTATION CONSIDERATIONS

Implementation of this bill would occur during the department's normal annual update of forms and instructions.

PROGRAM BACKGROUND

For federal purposes, an individual taxpayer who is qualified to exclude all of the gain from the sale or exchange of a principal residence (up to \$250,000 for single and \$500,000 for married filing joint) is not required to report the sale on the tax return. In addition, if gross proceeds from such a sale are less than \$250,000 (or \$500,00 in the case of a married couple), a report of the sale transaction (federal Form 1099-S, Proceeds From Real Estate Transactions) is not issued.

For purposes of filing thresholds, federal and state laws require that gross income be computed without regard to the exclusion for the sale or exchange of a principal residence. However, federal administrative practice has evolved to ignore gain from the sale of a principal residence that is excluded from gross income in determining the federal filing threshold. The Internal Revenue Service (IRS) personal income tax instructions no longer include gain on the sale of a principal residence as triggering the requirement to file a return. Additionally, when the gain on the sale of a principal residence is fully excludable and that gain alone would trigger a filing requirement, an IRS customer service representative will advise the taxpayer not to file a return.

OTHER STATES' INFORMATION

A discussion of how other states currently treat filing thresholds where only excludable gain would be reported is not relevant to the narrow application of this bill because the bill seeks to make California law consistent with IRS practice.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

This bill would not impact state income tax revenue.

POLICY CONCERNS

Repealing the requirement to include gain from the sale of a principal residence in gross income in determining whether the filing of a return is required would: 1) fulfill the department's goal of reducing taxpayer filing and compliance burdens; 2) eliminate unnecessary filing and storage of an indeterminable amount of information-only state income tax returns; and 3) avoid taxpayer confusion due to different federal and state treatment of gain on the sale of a principal residence in determining filing requirements.

LEGISLATIVE STAFF CONTACT

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